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Compliance Costs of Goods and Services Tax (GST) among Small and Medium Enterprises

(Kos Pematuhan Cukai Barangan dan Perkhidmatan (GST) di Kalangan Perusahaan Kecil dan Sederhana)

Rosiati Ramli
Mohd Rizal Palil
Norul Syuhada Abu Hassan
Ahmad Fariq Mustapha
(Faculty of Economics and Management, Universiti Kebangsaan Malaysia)

ABSTRACT

Taxation is one of the most important instruments in generating revenue for a country. History has shown that many countries develop based on tax revenue. Tax-based spending, also known as Goods and Services Tax (GST) or Value Added Tax (VAT) is a consumerism tax posed upon sales of goods and services. It is a potential tax instrument introduced by the Malaysian government in order to broaden and increase tax collection. The implementation of GST in Malaysia is a unique case in which it will replace service and sales taxes. The introduction of GST has had people from all walks of life, from academicians, professionals to the people (taxpayers), debating about the effect of increasing price and decreasing sales and services tax. The Malaysian government expects the GST to minimise individual and corporate tax rates in order to reduce tax liabilities in both entities. Small and medium enterprises (SMEs) are among the focal point of discussion related to the compliance cost of GST. The compliance cost of SMEs is expected to increase as soon as GST is implemented. As the profit of SMEs is relatively low, would they be able to adopt the initial compliance costs of GST efficiently at the time of its implementation? If the SMEs are receptive towards GST, how much are the compliance costs through new development of software system, training of human resources and new accounting system? The International Monetary Fund (IMF) believed that the Malaysian tax system could be enhanced (increased tax collection) by introducing GST. There are two main objectives of this study; first is to identify the compliance costs of SMEs in fulfilling their tax obligations; and second to investigate the expected costs and readiness of these companies in the implementation of GST. In achieving these two objectives, the data were collected from SMEs by using structured questionnaires. This study is significant as it estimates the compliance costs among SMEs as well as outlining recommendations and suggestions to tax administrators so that they could consider the tax liability and compliance cost in their daily operation.

Keywords: Compliance costs; small and medium enterprises; Malaysia; goods and services taxes (GST)

ABSTRAK

Cukai adalah instrumen yang penting dalam menjana pendapatan sesebuah negara. Sejarah telah membuktikan bahawa kebanyakan negara mampu membangun dengan hasil cukai. Cukai berasaskan perbelanjaan yang dikenali sebagai Cukai Barangan dan Perkhidmatan (GST) atau Cukai Nilai Tambah (VAT) merupakan cukai penggunaan yang dikenakan ke atas jualan barangan dan perkhidmatan. Ia merupakan salah satu instrumen percukaian yang diperkenalkan oleh Kerajaan Malaysia bagi mengembangkan dan meningkatkan kutipan cukai. Perlaksanaan GST di Malaysia merupakan kes yang unik di mana ianya menggantikan cukai jualan dan perkhidmatan. Pengenalan GST telah mengundang kritikan dari pelbagai pihak termasuklah ahli akademik, golongan profesional dan masyarakat (pembayar cukai) berkaitan kesannya ke atas peningkatan harga dan penurunan cukai barangan dan perkhidmatan. Kerajaan Malaysia menjangkakan pengenalan GST berupaya mengurangkan kadar cukai pendapatan individu dan korporat dalam mengurangkan liabiliti cukai kedua-dua pihak. Perusahaan Kecil dan Sederhana (PKS) menjadi titik fokal dalam perbincangan hang berkaitan dengan kos pematuhan GST. Kos pematuhan GST dijangkakan akan meningkat sebaik sahaja cukai GST dilaksanakan. Memandangkan kadar keuntungan di kalangan PKS adalah secara relatifnya rendah, mampukan mereka menyerap kos pematuhan permulaan GST terutamanya di peringkat awal pelaksanaan GST? Sekiranya PKS tersebut menerima pakai GST, berapakah pula jumlah kos pematuhan yang terlibat seperti pembangunan sistem komputer yang baru, latihan sumber manusia dan pembangunan sistem perakaunan? International Monetary Fund (IMF) percaya kecekapan sistem percukaian di Malaysia dapat ditingkatkan (meningkatkan kadar pungutan cukai) dengan pengenalan GST. Terdapat dua objektif utama kajian ini; pertama adalah untuk mengenal pasti kos pematuhan PKS dalam memenuhi obligasi cukai, dan kedua untuk menyiasat jangkaan kos dan kesediaan PKS ini terhadap perlaksanaan GST. Bagi memenuhi kedua objektif ini, data telah dikutip daripada syarikat PKS dengan menggunakan soal selidik berstruktur. Kepentingan kajian ini adalah untuk mendapatkan jangkaan kos pematuhan PKS terhadap penerimaan GST dan menyediakan cadangan kepada pihak berkuasa cukai supaya mengambil kira liabiliti cukai dan kos pematuhan untuk menghadapi operasi harian perniagaan.

Kata kunci: Kos pematuhan; perusahaan kecil dan sederhana; Malaysia; cukai barangan dan perkhidmatan (GST)

INTRODUCTION

Sales and Services Tax in Malaysia had been implemented on a certain range of products since 30th January 1975. However, from 1st April 2015, the sales and services tax was replaced with Goods and Services Tax (GST); which is defined as consumption tax imposed on the purchased of any kind of goods and/or services in a certain country. There have been lots of debates from various parties such as professionals and academicians on the influence of GST on the prices of goods and services in the future. The Malaysian government believed that the introduction of GST will increase the revenue and at the same time provide the government with an opportunity to reduce tax rates. However, will small and medium enterprises (SMEs) successfully adopt the systems efficiently with minimal compliance costs? The government charges an initial rate of 6% during the introduction of GST on 1st April 2015; replacing 10% and 6% of sales tax and services tax respectively. Mathematically, the 6% GST is lesser than cumulative 16% (10% plus 6%) of sales and service tax (SST) – transforming the prices of goods in lower tax rate as compared to previous tax regime of SST. However, whether there will be a decrease in the prices of goods from 1st April 2015 onwards is another issue to be discussed. Previous experiences have proven that retailers are reluctant to reduce prices of goods even though the government encourages them to do so. The present study has two main objectives. First, the study seeks to identify the compliance costs of SMEs in fulfilling their tax obligations. Second, the present study seeks to find out the estimated cost of implementing GST and investigate whether SMEs are prepared to comply with GST regulations. The data for this study were collected from SMEs by using structured questionnaires. The significance of this study is to estimate compliance costs among SMEs as well as outlining recommendations and suggestions to tax administrators so that they could consider the tax liability and compliance cost in their daily operation. The present study provides estimates concerning the compliance costs of SMEs following the introduction of GST and provides suggestions to tax authorities regarding the elements essential at minimising the compliance costs of SMEs. The findings of the study suggest that the compliance costs among SMEs in complying with GST are significant compared to the SMEs' projected net income. As the SMEs are generally comprised of small enterprises (sole proprietors), the initial compliance cost under GST is somewhat a burden to them. Judging from this finding, the Malaysian government should provide some tax incentives to compensate enterprises, particularly SMEs, for their initial compliance cost incurred as a result of the introduction of GST. The remainder of the present paper is structured as follows: the next section outlines the background of GST, followed by the issue and problems of GST, a survey of compliance costs and the manner in which such costs are estimated; the research design employed in the present study; the results of the present study; and finally the conclusion and implications of the present study.

BACKGROUND OF GST

Historically, GST was first introduced in Europe (France) in the 1950s. Currently, 160 countries in the world are using GST or VAT as the main component of national revenue. GST is a percentage of tax, at each stage of manufacturing where inputs are complimented with added value. In theory, the rate of GST in many countries is uniform, completely neutral to all forms of productive inputs. The operation of GST is considered as an input tax in which tax will be imposed on inputs processed to outputs. Many developed countries including the United Kingdom and New Zealand charge zero GST to basic needs products such as food, wheat, rice and public transport. The implementation of GST is based on a consumption-type tax in which tax will be imposed on all purchases of inputs from intermediaries. The OECD report in 2014 indicated that 160 countries in the world have implemented GST. Number of countries based on region is presented in Table 1 and GST in ASEAN countries is illustrated in Table 2.

TABLE 1. Number of countries with GST

Region	No. of Country
ASEAN	7
Asia	19
Europe	53
Oceania	7
Africa	44
South America	11
Caribbean, Central & North America	19

Source: http://www.treasury.gov.my/pdf/gst/list_of_countries.pdf

Based on Table 1 and 2, it was found that many countries have implemented GST especially in Europe and Africa. In ASEAN region, the data indicated that GST has been implemented as early as 1984 in Indonesia with an initial rate of 10%; while Laos is the most recent country in ASEAN that introduced GST in 2009 with an initial rate of 10%. Relatively, Singapore has the highest GDP per capita compared to other countries in ASEAN with USD46,241.00, followed by Malaysia with USD10,068.00; while Cambodia with initial 10% of GST rate in 1999 has the lowest GDP per capita with USD897.00. Judging from the information in Table 2, in particular, the implementation of GST in Malaysia is suitable and 'at the right time,' taking into consideration the GDP per capita and the initial rate of 6% within a stable economic condition. However, the comprehensive impact of GST toward the lower income earners is expected to be significant in influencing consumer behaviour, as many retailers as well as the citizens have low awareness of how GST will affect their daily transactions. Therefore, the government should

TABLE 2. GST in ASEAN countries

Country	GDP Per Capita (World Bank, 2013, USD)	Year of Implementation	Initial Rate (%)	Current Rate (%)
Indonesia	3,495	1984	10	10
Thailand	4,972	1992	7	7
Singapore	46,241	1993	3	7
Philippines	2,370	1998	10	12
Cambodia	897	1999	10	10
Vietnam	1,407	1999	10	10
Laos	1,320	2009	10	10
*Malaysia	10,068	2015	6	6

Source: http://www.treasury.gov.my/pdf/gst/list_of_countries.pdf

be prepared with the temporary impact on the economy as soon as the implementation of GST in April 2015.

ISSUES AND PROBLEMS OF GST

Many developed and developing countries have successfully implemented GST in their countries. GST as a consumption based tax has been able to widen the tax bracket compared to other taxes, i.e. income tax and wealth tax. However, the meaning of 'successful' is relatively wide and very subjective. Successful implementation of a new tax system can be measured based upon tax collection versus cost of collection efficiency, complexity of the new tax system, and the degree of acceptance among taxpayers (Smith 1776; Lymer & Oats 2008). Furthermore, compliance costs especially among SMEs play a significant role in determining the success of a new tax system. Unlike other developed countries such as United Kingdom, Australia and United States, Malaysia cannot continue requesting for debts to finance the deficits of its yearly national budget tabled in the Parliament. An approach is required to address the issues concerning deficits which lead to national budget deficits. The Malaysian government needs to manage the deficits in order to provide further opportunity for foreign direct investments in promoting special measures that can inspire and improve domestic economic stability, especially in the situation where world economic conditions are unfavourable. Malaysia has been experiencing fiscal deficits for five consecutive years, with GDP of 7% in year 2009. The number had decreased to 5.6% in 2010 while the Malaysian government estimates of less than 4% of GDP in 2015 (Bank Negara Annual Report 2013). Nevertheless, the government is attempting to restructure the subsidy scheme with the implementation of GST. The government is expected to collect MYR30 billion (USD8.33) of GST in the first year of its implementation in 2015. The extra revenue will be used to minimise the national deficits as well as sustaining Bank Negara Malaysia (National Bank of Malaysia) reserves as a preparation for future recessions and economic disasters.

HOW GST WORKS?

In Malaysia, unlike the SST, GST is levied on merchandises by individual manufacturer in the manufacturing and supply chain. A manufacturer enhances its resources or purchases before selling the new or improved merchandise or services to the customer or other business entities, providing added value. Upon retailing the merchandise or services, the company's distributor will include a small percentage of GST on the value of quantity sold. The company will then remit the GST collected from the previous sales (output tax) to the Customs Department after deducting the GST imposed on its purchases (input tax). This cycle continues throughout the supply chain.

Hence, GST is a multi-stage tax wherein it increases the sales price of the goods as they are transferred in the supply chain. GST is not charged on production, but on the consumption. The ultimate tax burden will be paid by the consumers rather than the retailer. In addition, some measures should be taken in order to minimise the impact of inflation. It is suggested that initial low rate for GST is vital and to increase the GST rate gradually over the future years. For example, Singapore imposed a rate of 3% during the first year of implementation and the rate increases gradually. Economists believed that the impact of inflation on the prices of goods prices depends on the operation of GST in a country as well as the people's purchasing power. The introduction of GST might call for a price increase of certain goods, and a price decrease in other products. Despite the huge challenges faced by any country during the first few years of GST implementation, the main concern of the Malaysians is whether the GST could possibly increase the final prices of goods and services.

According to Australian tax Office (ATO 2012), they found a significant impact on inflation in September 2000 as soon as GST was implemented in July 2000. There is an evidence of shock in national purchases several months before the implementation of GST. Many households rushed to purchase merchandises that they believed will be affected, i.e. those merchandises which prices will increase as a result GST. The study reported that inflation in Australia increased by 2.6% between July to September 2000. In addition, national consumption and economic undertakings declined as soon as GST was implemented; leading to slow economic growth, which resulted in economic decline during the first quarter of 2001. However, domestic purchases returned to normal after a few months in 2001.

In general, in order to have an effective impact on the economy during the initial period of GST implementation, the tax scheme shall include some compensatory procedures, including the decrease of personal and corporate income taxes as to increase consumption of household income and business entities. Besides, the system should be able to ensure that those lower and middle income earners, who may not fully enjoy the benefits of GST, are excluded from such payment in the GST tax system. Furthermore, the government should provide a special scheme especially for lower income group, for example GST-exempt for basic products as well as providing assistance programmes in order to lessen the burden of lower income group.

COMPLIANCE COSTS

In many tax jurisdictions, before implementing a new tax system or executing a tax reform, the government should seriously consider the compliance costs. Compliance costs is generally defined as "costs which are incurred by taxpayers [and] or by third parties in meeting the requirements of the tax system, over and above the tax liabilities itself and over and above any harmful distortions of consumption or production to which the tax may give rise" (Sandford et al. 1981: 13). Sandford et al. (1981) also outlined three separate elements to the costs of compliance; namely monetary/fiscal costs, time costs and psychological costs. Monetary costs include sums incurred on tax professionals (i.e. tax agents and accountants) and expenses relating to taxation guides, books, communication and other incidental costs. Monetary costs also include the initial (start-up) costs in forming a business entity, the cost of submitting GST returns, the cost of expertise in understanding and keeping up with changes in policies and rates, cost of external accountants for operational and advisory services as well as employee costs of running day-to-day GST accounting.

On the other hand, time costs are incurred by the taxpayer for completing tax return, preparing documentation to assist tax agents, maintaining business record for tax commitments, as well as time consumed by business entities for tax administration. In contrast, psychological costs exist and the onus is squarely on the business to conduct their GST activities appropriately alongside tax regulations; including financial and criminal sanctions for non-compliance with tax regulations and the costs of anxiety in complying with tax obligations.

The psychological costs of GST regulations can be very complex and many companies are aware that they lack the knowledge of the correct policies and transactional rates. This 'fear factor' is often highlighted as a component of compliance costs, even though it is not easily quantified. Tax compliance costs are frequently associated with the excess burden of taxation from economic point of view in which tax compliance costs are defined as any cost incurred, usually in complying with tax regulations. A study by Sandford et al. (1981) in the United Kingdom provides a significant finding of tax compliance costs for current literature. The study suggested that, first, there is a strong evidence to suggest that apart from economies of scale between business sizes, learning-by-doing also plays a crucial part in minimising the level of tax compliance costs; and secondly, it was obviously recognised that there are benefits, as well as costs, with tax compliance, and in turn, can be seen as giving greater gains to the more efficient firms.

However, the study by Sandford et al. (1981) did not explicitly elaborate on the overall source and time constraints of the learning-by-doing effect on tax compliance costs. Furthermore, with respect to tax compliance benefits, the study did not enquire the possibility of other gain provided by tax compliance (e.g. commercial benefits that might be derived from GST). Additionally, the study was also unable to provide a comprehensive assessment of which parties will pay tax compliance costs and what would be the impact on the revenues of firms and taxpayers. Such relevant areas of enquiry are incorporated in the present study.

Another point of view in relation to compliance costs is provided by Sandford (1976, 1973). He commented on issues related to the respective parties affected and also main forms of compliance costs. In spite of those issues, Sandford (1976) also adverted that incompatibility with tax operating costs might decrease a firm's revenue. Tax compliance costs need to be emphasised in the early stage of new tax system and further investigation will assist in providing better insights into problems relating to compliance costs. Businesses incur costs to comply with tax requirements, which add to their tax liability.

The method of book-keeping employed becomes a major problem relating to tax compliance costs for many traders. In Malaysia, the introduction of GST is mainly to increase national tax revenue and broaden tax bracket by taxing selected consumer purchases. A GST regime includes a significant transfer of taxpayers' tax incidence and responsibility of their compliance, whereby tax agents are expected to play a massive role by providing services during the initial year of GST implementation to taxpayers in complying with their tax obligations. In addition, as GST is expected to influence every entity particularly the SMEs, critical measures of intelligence should be implemented in order to ease the burden (compliance costs) of SMEs. The level of compliance costs will depend on several factors, namely occurrence of tax policy changes and simplicity of the tax laws. Hence, during the early years of GST implementation, compliance costs are expected to increase significantly especially among SMEs. Conversely, special consideration from the perspective of accountancy with regard to GST should take place before GST is implemented.

For example, GST payment posits a series of necessary duties closely associated to the regulations implemented by the Customs Department. The firms are also required to keep sufficient accounting records of all transactions for reimbursement purposes. Besides, the firms are required to provide supporting documents for their claims such as sales invoices, in line with the GST rules.

THE ESTIMATION OF COMPLIANCE COST

UK, USA and Australia are among the most advanced countries that had conducted researches in the area of compliance costs for over 20 years. Other countries including Hong Kong, Croatia, New Zealand, India, Spain, Malaysia and Singapore have also recently emphasised on tax compliance costs research.

Table 1 (measured per AU$1,000 of turnover), illustrates tax compliance costs for small commercials in New Zealand, UK and Australia. Based on the table below, they are at least nineteen times greater for both medium and large businesses (Evans et al. 1997: 79-80). Recently, Tax Impact Statement for tax law changes of requirements is a normal practice in the OECD countries. The countries include the European Union, Australia, the UK, New Zealand, and the US (Evans & Mike 1999: 21). The requirement to provide a Compliance Cost Assessment was introduced in 1985 in the UK; potentially turning the UK to be the earliest country to distinguish tax compliance costs as a significant issue (Sandford 1995: 3). Some major studies evidenced a regressive pattern of tax compliance costs (i.e. the burden falls heavily on smaller business entities).

TABLE 1. Tax compliance costs for enterprises income tax as a percentage of turnovers

Australia 1990/1991		New Zealand 1990/1991		UK 1986/1987	
Turnover (AU$ Million)	Compliance costs as a % turnover	Turnover (NZ$ Million)	Compliance costs as a % turnover	Turnover (£ Million)	Compliance costs as a % turnover
< 0.5	3.0	< 0.03	13.15	< 0.5	0.77
0.5 – 1	0.8	0.03 – 0.1	4.31	0.05 – 0.1	0.20
1 – 2	0.8	0.1 – 0.25	2.12	0.1 -0.5	0.17
2 – 5	0.2	0.25 – 0.5	1.35	0.5 – 1	0.07
5 – 10	0.1	0.5 – 1	0.78	1 – 10	0.03
10 – 20	0.02	1 – 2	0.79	10 and over	0.01
20 – 50	0.01	2 – 10	0.28		
50 and over	0.02	10 – 50	1.04		
		50 and over	0.03		

Source: Pope et al. (1994: 87)

TABLE 2. Tax compliance costs – corporate income tax per $1,000 turnover

Turnover Level/year (in HK$/S$/RM)	Hong Kong[a] 1995/1996	Singapore[b] 1994	Singapore[c] 1995	Malaysia[d] 1995
Less than 100 million	5.41	0.55	0.40	0.36
100-550 million	1.17	0.39	0.29	0.17*
More than 550 million	0.21	0.19	0.08	0.11*

Sources: [a]Chan et al. (1999: 55), [b]Ariff et al. (1995: 81), [c]Ariff et al. (1997: 1260), [d]Loh et al. (1997).
**Note*: the turnover level for Malaysia differs slightly, i.e. between RM100-RM500 million, and greater than RM500 million respectively.

TABLE 3. Tax compliance costs in Malaysia

Year of study	Public-listed company[a] 1995	SME[b] 1999
Tax Compliance Cost/per firm	RM68,836	RM21,964
Component of costs (%):		
Calculational	61%	59%
Planning	39%	41%
Sources of costs (%):		
Internal	28%	75%
External	72%	25%

Source: [a]Loh et al. (1997) and [b]Hanefah et al. (2001)

In Australia, GST was introduced on 1st July 2000 and raised many arguments, particularly with regard to the effects on lower income earners. The principal argument is that the tax consumes a higher proportion of income in low income households when compared against higher income earners. However, the problems were resolved by reductions in personal income taxes, state banking taxes, federal wholesales tax and some fuel taxes that were implemented when the GST was introduced. Furthermore, as a result of the rush by consumers to purchase goods perceived to be potentially extra expensive following the introduction of the GST as mentioned above, consumer consumption and economic growth declined to such extent that the Australian economy recorded negative economic growth for the first time in more than 10 years at the end of the first fiscal quarter of 2001, i.e. after the GST came into effect. As a result, the Australian government was criticised by small business owners over the increased administrative responsibilities of submitting Business Activity Statements (BAS) on a quarterly basis to the Australian Taxation Office (Queensland University of Technology 2006).

In New Zealand, the GST was first introduced on 1st October 1986 at a rate of 10% for most services and goods. In July 1989, the rate was increased to 12.5% and increased again to 15% on 1st October 2010. The GST in New Zealand was also introduced in conjunction with compensatory changes to personal income tax rates. Similar to the implementation of the GST in Australia, the consumers in New Zealand were also anxious prior to the introduction of the GST. Many consumers were worried about the impact of the tax on their cost of living. The New Zealand tax authority complemented the introduction of GST with a reduction in personal progressive income tax rates so that the tax incidence among consumers would be balanced (Giles 2000).

Issues pertaining to GST during the early stage of implementation are inevitable. Judging from the experience of other countries including Australia and New Zealand, consumers perceived that the introduction of GST will increase their living costs significantly and subsequently oppose the implementation of GST. On the other hand, from the perspective of political stability, the opposition party of the current government will always oppose the introduction of GST. Theoretically, the introduction of any new tax instrument by a government will benefit a country as the revenue will increase and income redistribution can be accomplished efficiently and effectively. In addition, the low income earners will benefit as a result of income redistribution through a variety of mechanisms such as subsidies, infrastructure and health services (Smith 1776). Therefore, looking at the scenario in Australia and New Zealand at the early stage of GST implementation as a benchmark to other countries such as Malaysia which pursues to widen its tax regime, it will collect extra revenue and finally benefit the nation in the long run.

WHAT IS SMALL AND MEDIUM ENTERPRISES?

According to Small and Medium Enterprises Corporation (SMECorp) of Malaysia, an enterprise is considered an SME in each of the respective sectors based on the annual sales turnover or number of full-time employees. SMEs can be classified into two main categories; manufacturing and services. Services SMEs are defined as "*small and medium enterprises in the services, primary agriculture and Information and Communication Technology (ICT) sectors with full-time employees not exceeding 50 or with annual sales turnover not exceeding RM5 million*." Manufacturing SMEs are defined as "*small and medium enterprises in the manufacturing related services and agro-based industries with full-time employees not exceeding 150 or with annual sales turnover not exceeding RM25 million*." Table 4 illustrates the definitions of SME from tax perspectives.

TABLE 4. SMEs definition for tax purpose

Types of incentives/deductions*	Definition of small and/or medium enterprises
A dual corporate tax rates.	Company (resident in Malaysia) with an ordinary paid-up capital up to RM2.5 million at the beginning of the basis year.[a]
Deductions for pre-incorporation expenses.	Company (incorporated in Malaysia) and having authorized capital of not more than RM2.5 million.[b]
Pioneer status or investment tax allowance.	A small-scale company (incorporated in Malaysia) with a shareholder's funds not exceeding RM500,000.[c]

**Note*: Other requirements may apply. For example, incentive for a small-scale company is confined to manufacturing sectors with at least 60 per cent Malaysian equity.

Sources: [a]Para 2A, Schedule 1, ITA 1967; [b]Para 2(1) Income Tax (Deduction for Incorporation Expenses) Rules 2003; [c]Guidelines and Procedure for Applying Tax Incentive for Small Scale Manufacturing Companies under the PIA 1986.

RESEARCH METHODOLOGY

QUESTIONNAIRE DESIGN

The survey instruments were developed based on the studies by Abdul Jabbar (2009) and Junainah (2002) and divided into four main sections. The first section is consisted of background information concerning the SMEs, including their main business activity, turnover, and profit and tax liability. The second section is consisted of a series of questions pertaining to respondents' compliance costs of corporate taxes which include both internal and external costs. In order to identify the expected compliance costs of GST, the third section of the questionnaires posed several questions concerning their employee wages, expected average hours consumed by tax employees within a week, and their salaries. Their potential expenses due to GST implementation were also included in the survey.

The last part of the questionnaire requires the respondents' feedback pertaining to the awareness, readiness and impacts of GST on SMEs. A study by Junainah (2002) attempted to obtain business entities' awareness, readiness and perceptions toward the Self-Assessment System (SAS); a new tax system implemented in 2004. Junainah's study was conducted several years prior to the implementation of SAS. Therefore, the utilisation of Junainah's approach and instrument is relevant to the present study. Present study analysed 173 samples of SME businesses in order to answer the research objectives as well as research questions. The results of the present study are discussed in the next section by outlining the descriptive evidence and calculation of tax compliance costs among SMEs.

DATA COLLECTION

Consistent with the scope of the present study on GST implementation among SMEs, the sample frame was drawn from both manufacturing and service sectors. A structured survey among SMEs throughout Malaysia was done and respondents were chosen randomly from various business entities. The classification of the samples is based on criteria suggested by the SME Corporation Malaysia (http://www.smecorp.gov.my). The total population of SMEs according to SME Corp is 548,266, comprising 434,938 entities which earned an annual sales turnover of less than RM250,000.00 (classified as micro category). This group of entities is not likely to be influenced by the GST. Another 113,329 entities were then classified as services, manufacturing and agriculture. Agricultural industries related with foods were excluded from the sample due to GST exempt items. Therefore, 110,977 SMEs of the manufacturing and services sectors were included as samples for the research.

Samples of 1,108 SMEs were considered suitable to provide reliable and valid data analysis. In contrast, it should be noted that low response rate (i.e. less than 20%) is normal for any study conducted in Malaysia. For example, Che Rohana and Foong (2005) only obtained a 10% response rate, while Ruzita et al. (2007) managed to get 12% response rate. Ruzita et al. (2007: 125) further asserted that "for a mail survey a low response rate is not unusual in Malaysia." A target response rate of 10 percent would mean a total of at least 111 replies.

Since the survey examines the compliance costs of SMEs in response to the introduction of GST, this study employed enumerators as the primary data collection method. The presence of the enumerators is expected to establish multiple interactions so that the issues of the survey could be directly addressed to the respondents. Although the use of enumerators is costly compared to other data collection methods such as mail surveys and interviews, Black et al. (2001) asserted that this method is the most suitable in obtaining a valid, reliable and independent data.

DATA ANALYSIS

The study has successfully collected 173 responses from respondents of SMEs of various industries including manufacturing, services and both manufacturing and services. Some sensitive and difficult questions particularly concerning monetary costs and implementation of GST were not completely answered by the respondents. The descriptive analysis is provided in the present section concerning the background of the SMEs, issues in GST monetary compliance costs and the potential impacts of GST on business entities. The analysis revealed that responses were obtained from companies located in East Malaysia (26.6%), Central Region (24.3%), Eastern Region (19.7%), Southern Region (16.2%), and the Northern Region (13.3%). Meanwhile, most of the SMEs were involved in the service sector (71.7%) and followed by the manufacturing sector (28.3%). From the analysis, 53 of the SMEs were liable for services tax while 95 of the SMEs were liable for sales tax. Only 25 SMEs were not subjected to sales and services tax. In terms of accounting profit in 2010, 82.2% of the SMEs were in the first four levels, which gained between zero profit and RM300,000.00. As for the turnover in 2010, 56.7% of the SMEs earned between RM200,000.00 and RM500,000.00. Conversely, 3.0% of the SMEs reported profit of above RM4 million. Out of these, more than half (60.9%) of the SMEs had a tax liability below RM20,000.00 (40.2%), while 20.7% of the SMEs carried no tax liability. 44.5% of the respondents clearly asserted that they will be subjected to GST, while 43.4% of the respondents were unsure as to whether they will be subjected to GST. Only 12.1% of SMEs stated that they will not be subjected to GST.

The findings of the study are discussed in two parts. The first part examines the current compliance costs (internal, external and additional costs) incurred by the SMEs relating to corporate income tax. Since the proposed GST is yet to be implemented in Malaysia, the current compliance costs relating to corporate income tax is significant since it will be used as a base to determine the expected compliance costs incurred following the implementation of the proposed GST. The expected compliance costs incurred by SMEs as a result of the implementation of GST will be examined in the second part.

COMPLIANCE COSTS OF CORPORATE INCOME TAX

EXTERNAL COMPLIANCE COST

External costs can be defined as payments made to obtain financial services from various parties such as the professionals in the areas of accountancy, tax, legal, and investment; all of whom are external parties to the business entities. In this study, the result showed that most of the SMEs required professional financial services namely accounting services (40.1%), tax services (26.5%) and both tax and accounting services (12.9%).

Majority (62%) of the SMEs in this study indicated that the main explanation for utilising external professional tax services was due to the lack of technical knowledge in the area and also cost effectiveness; about 29% of the respondents stated it is in compliance with their company policy; while the remaining 9% responded to a combination of the aforementioned reasons. In terms of the amount paid, the average amount that SMEs in this study incurred in 2010 was RM7,388.00 for tax related services; out of which RM3,222.00 was for tax planning, RM2,103.00 for tax calculation, and RM2,063.00 for tax appeal.

INTERNAL COMPLIANCE COST

Internal costs of compliance can be defined as the money and time consumed by business personnel in preparing and maintaining accounting and taxation material for tax agents and accountancy experts. The findings of the study showed that accounting team consumed extra time on tax issues (6.72 hours per week (hpw)), manager (6.60 hpw) and computer team (5.16 hpw). Accounting team consumed extra time on tax calculation and the managers consumed extra time on tax appeal and planning. Conversely, IT experts consumed the least amount of their time in relation with tax calculation, planning and appeal compared to the others. The study also found evidence that managers were paid the most wages, nearly RM4,166.00 per month, followed by accounting team and IT experts at RM2,770.00 and RM1,632.00, respectively.

The study also found that the average internal compliance cost of SMEs in this study is at RM16,722.00. The figure was calculated by multiplying the annual time consumed on tax undertakings by managers, accounting members as well as IT team with their wage rate per hour. It is shown in Table 5 below.

TABLE 5. Calculation of internal tax compliance cost

	Hours consumed per week (a)	Average working hours per week (b)	Salary per week RM (c)	Annual tax compliance cost RM (d) = (a/b) × c × 52 weeks
Managers	6.60	45	1,041	7,939
Accounting team	6.72	40	692	6,045
IT team	5.16	40	408	2,737
Total				16,722

ADDITIONAL COST COMPLIANCE COST

This study also emphasised on the costs spent by the SMEs relating to corporate tax issues, including substantial purchasing tax and staff training on tax issues, and other expenses including travel, postage, stationary, and photocopying. Such costs are referred to as additional costs since they are internal costs relating to a non-team matter. It was found that on average, the SMEs incurred a total extra cost of RM4,297.00 on tax issues, with the most expenditures utilised on human resource training (RM1,552.00), followed by buying tax materials (RM1,461.00) and other miscellaneous expenses of RM1,283.00.

TOTAL TAX COMPLIANCE COST ESTIMATIONS

The compliance cost estimate employed in this study follows similar approaches in extant studies. Based on the analysis above on the external, internal and additional cost of compliance on corporate tax, this study showed that the total average compliance cost per SME in 2010 was RM28,406.00 annually per firm, which encompasses internal cost of RM16,722.00 (or 58.87%), external cost of RM7,388.00 (26.01%), and additional cost of RM4,296.00 (15.12%) of the total compliance cost.

EXPECTED COMPLIANCE COSTS OF GST

External Cost This study then investigated the expected compliance costs of GST among SMEs. As soon as GST is implemented, a significant number of SMEs believed that they will appoint external services from experts for their tax calculation (70.5%), and tax calculation and planning (10.3%). Similarly, the SMEs expected to incur extra cost of RM6,337.00 on GST services provided by external professional services per year; RM2,687.00 for planning, RM2,007.00 for tax calculation, and RM1,644.00 on tax reconsideration.

Internal Cost Besides the external cost, most of the SMEs in this study forecasted that GST will potentially increase SMEs' internal compliance costs, particularly tax calculation, planning, and tax appeal. 58% of the respondents felt that the implementation of GST would increase their tax calculation, 29% responded that it increases tax planning, and 12% forecasted increases in tax appeal.

Additional Cost In terms of additional costs in complying with GST, this study also found that most SMEs in this study were still not prepared for the implementation of GST. This is because only 13 (7.5%) had purchased GST tax guide and software and only 17 (9.8%) SMEs had invested in human resource training concerning GST. The rest of the respondents were unsure of what to prepare and the expected additional cost incurred.

DISCUSSION AND CONCLUSIONS

As stated in the earlier section, the main objective of this paper is first to find out the compliance costs of SMEs in fulfilling their corporate tax obligation, and secondly to investigate the expected costs and readiness of these companies toward the implementation of GST. In relation to the first objective, this study suggested that the average tax compliance cost per SME in 2010 was RM28,407.00 annually per company, which encompasses internal cost of RM16,722.00 (or 58.87%), external cost of RM7,388.00 (26.01%), and additional costs of RM4,296.00 (15.12%) of the total compliance cost. With the implementation of GST, the study also showed that the SMEs expected the external source of GST services with an estimated average external cost of RM6,336.00 per year. This could mean that for SMEs to comply with both the corporate tax and GST, the compliance cost would be at least RM34,742.00 (RM28,406.00 + RM6,336.00). This does not include the internal cost and additional cost of complying with the GST. Nevertheless, the study found that the SMEs were expecting these costs to increase with the implementation of GST, particularly tax calculation, tax planning, and tax appeal.

As for the impacts of the implementation of GST on SMEs, majority of the SMEs participated in the study agreed that their businesses would continue as usual with turnover and profit continue to increase despite the implementation of GST. Nevertheless, many believed that their tax responsibility is going to increase alongside administrative procedures, which may affect their business performance. The present study expects a significant increase in compliance cost to potentially occur during the first five years, in a fashion similar to the introduction of SAS in 2001. Soon after the introduction of SAS in year of assessment 2001, the compliance cost of SMEs during the first five years (2002 to 2006) had increased, albeit at diminishing marginal increment. The compliance costs for SAS later decreased as the majority of enterprises were able to acclimatise to their tax obligations. The decrease of compliance costs among SMEs in relation to the SAS was not due to the efforts of the SMEs alone. In fact, the Inland Revenue Board of Malaysia (IRBM) contributed significantly to the decreased compliance costs through various measures, including the simplification of the tax system via a substantial reduction of capital expenditure categories for capital allowance purposes; simplification of business basis period; and introduction of dual interest rates for SMEs.

When asked whether they are ready for the implementation of GST, most SMEs were still not prepared for the implementation of the GST. The study showed only 13 SMEs in this study had invested in GST's tax guide and software, while only 17 SMEs had invested in human resource training concerning the GST. This finding implies that majority of the SMEs will need to allocate extra fund on human resource training during the early stage of the implementation of GST, which is considered as an additional burden to small and medium enterprises.

In the last section of the questionnaires, a series of questions enquired whether the respondents received necessary information and promotions from the tax authorities about the intended GST system and its mechanism. The result showed that respondents appeared to not have received sufficient information and promotions from the tax authorities. Many respondents were still unsure on how the GST will be implemented. The implication to the management is that the Malaysian government should further promote the GST through media and other channels so that SMEs are aware of the actual impacts of GST. The government should also provide tax policies in place, including lowering the income tax rates or increasing tax benefits to SMEs, to reduce the burden of SMEs in fulfilling their tax responsibilities.

Despite the fact that GST would increase compliance costs of SMEs, the experience of other countries which have already implemented GST, indicates that the introduction of GST has improved their tax revenues and efficiency. It is believed that the decision by Malaysian government to implement GST in early 2015 would remove the inefficiencies and redundancies of the current sales tax and service tax in Malaysia. Nevertheless, the expected compliance cost of GST among SMEs in Malaysia requires further research, particularly with regard to examining the relationship between compliance costs and non-compliance behaviour of SMEs following the implementation of GST.

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Rosiati Ramli (corresponding author)
Faculty of Economics and Management
Universiti Kebangsaan Malaysia
43600 UKM Bangi, Selangor, MALAYSIA.
E-Mail: rosie@ukm.edu.my

Mohd Rizal Palil
Faculty of Economics and Management
Universiti Kebangsaan Malaysia
43600 UKM Bangi, Selangor, MALAYSIA.
E-Mail: mr_palil@ukm.edu.my

Norul Syuhada Abu Hassan
Faculty of Economics and Management
Universiti Kebangsaan Malaysia
43600 UKM Bangi, Selangor, MALAYSIA.
E-Mail: syuhada@ukm.edu.my

Ahmad Fariq Mustapha
Faculty of Economics and Management
Universiti Kebangsaan Malaysia
43600 UKM Bangi, Selangor, MALAYSIA.
E-Mail: afariqmustapha@yahoo.com